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No. 93-

Supreme Court, U.S.
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IN THE

Supreme Court of the United States

OCTOBER TERM, 1993

OLIN CORPORATION
Petitioner,

v.

FEDERAL TRADE COMMISSION
Respondent.

Petition for a Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit

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PETITION FOR A WRIT OF CERTIORARI

NEAL R. STOLL
Counsel of Record
JAMES A. KEYTE
ALAN J. MEESE
Skadden, Arps, Slate,
Meagher & Flom
919 Third Avenue
New York, New York 10022
(212) 735-3000
Counsel for Petitioner

QUESTIONS PRESENTED

1. Whether the Court of Appeals correctly applied the doctrine established by this Court in *United States v. General Dynamics Corp.*, 415 U.S. 486 (1974)?

2. Whether the Court of Appeals correctly held that, under this Court's decision in *Brown Shoe Co. v. United States,* 370 U.S. 294 (1962), two products can occupy the same antitrust product market even though there is an undisputed lack of meaningful cross-elasticity of demand between them?

3. Whether the Court of Appeals violated established principles of administrative law in extracting the Federal Trade Commission from the analytical flaw known as the "Cellophane trap"?

4. Whether it was punitive for the Court of Appeals to affirm a Section 7 remedy that directly contradicts the court's basis for upholding Section 7 liability?

PARTIES TO THE PROCEEDING

The only parties to the proceeding are those that appear in the caption.

STATEMENT PURSUANT TO RULE 29.1

Olin Corporation has the following subsidiaries that are not wholly owned: Aegis, Inc.; Aquachlor (proprietary) Limited; Asahi-Olin Ltd; Babcock & Wilcox Idaho, Inc.; Chlor-Chem Limited; Egide, S.A.; Empire of Carolina, Inc.; Etoxyl, C.A.; Fuji-Hunt Electronics Technology Co., Ltd.; Indy Electronics De Mexico, S.A. de C.V. (dormant); The Industrial Credit and Investment Corporation of India Limited; International Disarmament Corporation; Kyodo TDI Limited Company; Niachlor; Nordesclor S.A.; OCG Holdings, Inc.; OCG Microelectronic Materials AG; OCG Microelectronic Materials GmbH; OCG Microelectronic Materials, Inc.; OCG Microelectronic Materials Limited; OCG Microelectronic Materials N.V.; OCG Microelectronic Materials S.A.; OCG Microelectronic Materials S.R.L.; OIT Holding Corporation (dormant); Olin-Asahi Interconnect Technologies (a partnership); Olin Pantex Inc. (in process of dissolution); Pisgah Partners II; Productora De Alcoholes Hidratados, C.A. (PRALCA); Purified Acid Partners (a partnership); Sukulu Mines Limited; Techniche Olin Limited; Tortuga Casualty Company; U.S. Shippers Association; Yamaha-Olin Metal Corporation.

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PETITION FOR A WRIT OF CERTIORARI

Olin Corporation hereby petitions for a writ of certiorari to review the judgment of the United States Court of Appeals for the Ninth Circuit in this case.

OPINIONS BELOW

The opinion of the Court of Appeals (App. 1a-30a) is reported at 986 F.2d 1295 (9th Cir. 1993). The opinion of the Federal Trade Commission (App. 31a-76a) is not reported.

The order of the Court of Appeals denying rehearing is not reported.

JURISDICTION

The judgment of the Court of Appeals was entered on February 26, 1993. A timely petition for rehearing was denied on August 12, 1993. The jurisdiction of this Court is invoked under 28 U.S.C. § 1254(1).

STATUTORY PROVISIONS INVOLVED

Section 7 of the Clayton Act, 15 U.S.C. § 18, provides in pertinent part:

> No person engaged in commerce . . . shall acquire, directly or indirectly, the whole or any part of the stock or . . . assets of another person . . . where in any line of commerce . . . the effect of such acquisition may be substantially to lessen competition, or to tend to create a monopoly.

Section 706 of the Administrative Procedures Act, 5 U.S.C. § 706, provides in pertinent part:

> [T]he reviewing court shall decide all relevant questions of law. . . . The reviewing court shall —
>
> . . . .
>
> (2) hold unlawful and set aside agency action, findings, and conclusions found to be —
>
> (A) arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with law. . . .

STATEMENT

The instant case presents this Court with an important opportunity to clarify the law governing the analysis of mergers under Section 7 of the Clayton Act, in particular the meaning of the doctrine established in *United States v. General Dynamics Corp.*, 415 U.S. 486 (1974), and the standards governing product market definition. The time has long been ripe for such clarification.

This Court last spoke to *General Dynamics* 18 years ago, see *United States v. Citizens & Southern National Bank*, 422 U.S. 86 (1975), and has not had occasion to pass on the standards governing product market definition in the merger context for nearly two decades. *See General Dynamics*, 415 U.S. 486. Indeed, there can be little doubt that the absence of recent guidance from this Court on these issues contributed to the Ninth Circuit's departure from prevailing precedents in this case.

This case concerns the attempt by Olin Corporation ("Olin") to become a competitive producer of chlorinated isocyanurate pool sanitizers ("isos"). Isos are the latest and most convenient of three chlorinated chemicals used to kill algae and bacteria in swimming pool water. The other two chlorinated chemicals used to sanitize pool water are calcium hypochlorite ("cal hypo") and liquid bleach.

The greater convenience and efficacy of isos is reflected in an approximately 100% price premium for isos over cal hypo. The critical ingredient exclusive to isos that accounts for its superior performance is a stabilizer, cyanuric acid ("CA"). CA, in turn, accounts for approximately 50% of the cost of isos production. (App. 2a) Not surprisingly, the parties stipulated, and the FTC found, that isos

constitutes its own relevant product market under Section 7 of the Clayton Act. (App. 6a)

In the late 1970s, Olin, recognizing the significance of the emerging isos market, endeavored to become a fully integrated producer of isos similar to all of its isos competitors. After encountering serious and prolonged technical problems, and losing tens of millions of dollars, Olin shut down its CA plant in 1980. Olin, however, attempted to continue to produce isos between 1981 and 1984 using CA purchased from an isos competitor, Nissan, the only producer of CA capable and willing to sell CA to Olin. Nissan, however, as would any firm in a monopolistic supply relationship, charged Olin supracompetitive prices for CA.

In order to escape from its dependence on Nissan for CA, in 1984 Olin entered into a contract manufacturing agreement with another isos competitor, Monsanto Company, and ceased its isos production. From the time that Olin shut down its CA plant and became dependent on its isos competitors, Olin was no longer a competitively viable isos producer.

In early 1985, Olin entered into an agreement to purchase FMC's integrated isos business. Although the FTC challenged the FMC transaction, it apparently recognized Olin's lack of viability as an isos producer by permitting the acquisition to go forward subject to an asset maintenance agreement.[1]

After several years of litigation, the FTC eventually found that the acquisition violated Section 7 of the Clayton Act, 15 U.S.C. § 18, in the stipulated isos market and in a

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[1] Under that agreement, Olin was required to maintain the FMC assets in a state of productive readiness during the pendency of the litigation.

broader product market defined as "dry sanitizers." (App. 46a) A necessary predicate to the FTC's decision that the FMC acquisition substantially lessened competition in any relevant market was its incorrect finding that Olin was a fully viable producer of isos, notwithstanding its utter failure to produce the critical CA input. Also flawed was the FTC's definition of a "dry sanitizer" market comprised of isos and cal hypo. The FTC defined this broad market even though isos and cal hypo admittedly lacked significant cross-elasticity of demand under the Supreme Court's test in *Brown Shoe Co. v. United States,* 370 U.S. 294 (1962).

Finally, and ironically, the FTC ordered Olin to divest its CA plant to ensure the "viability" of the acquiring entity, even though the FTC had predicated its finding of Section 7 liability on the basis that Olin was a fully viable isos producer without the ability to manufacture its own CA.

The Ninth Circuit panel affirmed the FTC's legally deficient decision by misconstruing several fundamental antitrust and administrative law doctrines established by this Court. As a result, the Ninth Circuit is now in direct conflict with the decisions of this Court and numerous other Circuit Courts of Appeal.

First, the panel's decision reflects a complete lack of understanding of this Court's decision in *United States v. General Dynamics Corp.,* 415 U.S. 486 (1974), and the decisions of other circuits applying *General Dynamics*. This body of precedent stands for the proposition that a firm's historic market share must be discounted to reflect its inability to produce or sell a product competitively. The panel found, however, that Olin was an independent, competitive

isos producer even though it agreed that (i) Olin failed dismally in its attempts to produce CA, the key input for isos, and (ii) Olin was unable to purchase CA except on a limited basis from one competitor, Nissan, which stood in a monopolistic supply relationship to Olin. (App. 3a) The panel therefore incorrectly relied on Olin's historic isos market share in affirming the FTC's finding of the transaction's anticompetitive effects.

Second, the panel's decision sustaining a "dry sanitizer" product market directly conflicts with the standard established by the Supreme Court in *Brown Shoe* to determine the outer boundaries of an antitrust product market. Erroneously deferring to the FTC on a purely legal question, the panel held that two products can occupy the same antitrust product market even though the cross-elasticity of demand between those products is "somewhat inelastic." This conclusion flowed inexorably from the panel's refusal to place any limit on the hypothetical price increase used to determine whether consumers would substitute one product for another in response to an increase in the price of the latter.

Absent such a limitation, the integrity of the *Brown Shoe* cross-elasticity of demand analysis is destroyed. As Judge Hand recognized long ago, a large enough price increase will induce substitution away from any product. *United States v. Aluminum Co. of America*, 148 F.2d 416, 426 (2d Cir. 1945). Moreover, the panel's approach directly conflicts with those decisions holding that two products cannot occupy the same market unless there is a *high* cross-elasticity of demand between them and that, in determining whether meaningful cross-elasticity exists, courts should hypothesize a *small* price increase. *E.g., United States v.*

Archer-Daniels-Midland Co., 866 F.2d 242, 248 & n.1 (8th Cir. 1988), *cert. denied,* 493 U.S. 809 (1989).

In holding that "relatively inelastic" cross-elasticity over a long period of time is sufficient, the panel accepted the FTC's rationale that the presence of other factors—notably, the purported similar physical characteristics of isos and cal hypo—could supplant the economic rigor required by the decisions of this Court to define antitrust markets. Again, this result stands in stark contrast to the position taken in other circuits, namely, that the so-called *Brown Shoe* factors possess no independent significance in and of themselves. *E.g., Rothery Storage & Van Co. v. Atlas Van Lines, Inc.*, 792 F.2d 210, 218-19 (D.C. Cir. 1986) (Bork, J.), *cert. denied,* 479 U.S. 1033 (1987).[2] Moreover, the application of a boundless cross-elasticity standard should have resulted in the inclusion of the third chlorinated pool sanitizer, liquid bleach, in the relevant product market.

Third, even if the panel was correct in holding that "somewhat inelastic" cross-elasticity of demand suffices to bring two products into the same antitrust product market, the panel erred as a matter of law in sustaining the FTC's conclusion that even low cross-elasticity of demand was present in this case. Specifically, the FTC's finding that some consumers would shift from cal hypo to isos was premised on data distorted by the artificial depression of

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2 The ramifications of these conflicting standards go well beyond the merger context. Market power, and thus market definition, is an essential element in many antitrust contexts, *Jefferson Parish Hospital District No. 2 v. Hyde,* 466 U.S. 2, 26-29 (1984) (market power a necessary condition for finding of *per se* illegal tying), and this Court has held that the same standards that govern market definition under Section 7 of the Clayton Act govern such definition under the Sherman Act. *United States v. Grinnell Corp.*, 384 U.S. 563, 572-73 (1966).

isos prices that resulted from the dumping of isos on the domestic market by Japanese producers. Thus, the FTC fell into a variation of the so-called "Cellophane trap" by calculating cross-elasticities between two products at non-competitive prices.[3] The panel did not dispute that the FTC had made this analytical error. (App. 16a)

In extracting the FTC from the "Cellophane trap," however, the panel violated well-settled principles governing the allocation of responsibility between courts and administrative agencies. Specifically, the panel rescued the FTC from the "Cellophane trap" by accepting, *ex post facto*, FTC counsel's rationale for finding cross-elasticity between isos and cal hypo even though the price of the former was artificially depressed. Summary reversal is therefore warranted. *See SEC v. Chenery Corp.,* 318 U.S. 80 (1943).[4]

Finally, and no less significant, the panel's decision raises serious and far reaching questions regarding the scope of permissible relief under Section 7 of the Clayton Act and

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[3] The "trap" is so named for this Court's decision in *United States v. E.I. du Pont de Nemours & Co.,* 351 U.S. 377 (1956), where this Court unwittingly measured the cross-elasticity between two products—cellophane and other "flexible packaging materials"—in circumstances in which cellophane was already at a monopoly price and substitution with other products thereby began to occur. Such an approach is inconsistent with this Court's recent holding that high cross-elasticity between a product priced at non-competitive levels and its substitutes does not suggest that the products occupy the same market. *Eastman Kodak v. Image Technical Servs., Inc.,* 112 S. Ct. 2072, 2084 (1992). *See* A.B.A. 1992 Annual Review of Antitrust Law Developments, 81 & n.9 (1992).

[4] The panel also improperly affirmed the FTC's decision even though it could not determine the rationale of the FTC's decision, i.e., could not determine in which market the FTC found anticompetitive effects. (App. 7a) *Burlington Truck Lines, Inc. v. United States,* 371 U.S. 156, 167-68 (1962).

the need for consistency between the relief ordered and the theory of liability. In particular, if the *General Dynamics* doctrine was correctly applied by the panel—i.e., Olin was a fully viable isos producer without a captive CA supply—the panel was incorrect in upholding the FTC's order requiring Olin to divest the CA plant purchased from FMC "in order to ensure the *viability* of the divested entity as an isos producer." (App. 30a) (emphasis added) Furthermore, since Olin's viability as an isos producer was predicated on the benevolence of its competitors, at a minimum the panel should have remanded the case for consideration of whether a Nissan CA supply relationship, or a Monsanto contract manufacturing agreement, remains an available option for Olin nearly a decade after the FTC permitted the parties to merge subject to the asset maintenance agreement. Indeed, it is punitive and in no way remedial under Section 7 of the Clayton Act to render Olin an ineffective competitor in favor of a speculative competitive entity created as a result of divestiture.

REASONS FOR GRANTING THE PETITION

I. THE PANEL IGNORED THE *GENERAL DYNAMICS* DOCTRINE

The panel upheld the FTC's finding that, independent of its acquisition of FMC, Olin had been a fully viable and independent producer of isos.[5] The panel held that, despite Olin's inability to produce CA, it was still a fully viable isos producer because Olin was able to purchase CA from one of

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5 The panel agreed with Olin that, were this finding erroneous, the FTC's ultimate finding of anticompetitive effects in the "dry sanitizer market" could not be affirmed since the market share assigned to Olin would overstate its pre-acquisition competitive significance. (App. 8a & n.9)

its integrated competitors, Nissan.[6] (App. 26a) This approach, which essentially renders the *General Dynamics* doctrine meaningless in the Ninth Circuit, contradicts the decisions in other circuits and this Court that have interpreted *General Dynamics* flexibly to account for any circumstance in which a firm's current or future competitive significance is questionable. Moreover, applying the panel's reasoning, *General Dynamics* itself was wrongly decided by this Court.

General Dynamics involved a challenge to a merger in which the government's assertion of anticompetitive effects had been based on historic market shares in the production and sale of coal. 415 U.S. at 494-96. The *General Dynamics* Court held that these historic market shares were poor

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[6] A related basis for granting certiorari in this case is that the panel incorrectly permitted the FTC to saddle Olin with the burden of persuasion, rather than a mere burden of coming forward, relating to the viability issue. *See United States v. Baker Hughes Inc.*, 908 F.2d 981, 991 (D.D.C. 1990) (under Section 7, the burden of persuasion always remains with plaintiff). Thus, the FTC required Olin to make "a persuasive showing" that Olin was not a viable isos producer and establish "with certainty" that it had no alternatives to the acquisition. (App. 57a-59a) The panel attempted to minimize the FTC's mistake on the ground that *Baker Hughes* involved a more egregious shifting of the burden of proof. (App. 25a) But this is beside the point: Olin did come forward with an overwhelming amount of evidence on its lack of full viability as an isos producer and FTC counsel, contrary to the panel's assumption, never even purported to make a persuasive showing that Olin was fully viable. Indeed, FTC counsel maintained below that the burden had never shifted back to the FTC to make such a showing.

indicators of United Electronic's competitive significance in the marketplace because the firm's relatively depleted reserves were already committed for sale under long-term contracts. 415 U.S. at 502-03, 506-10. Because the firm had no control of its future output, i.e., coal production, its elimination from the marketplace could have no significant anticompetitive effect. *Id.* at 502-03. As Judge Easterbrook has explained:

> The real 'owners' of the coal currently being delivered were the recipients under the contracts, not the sellers. One of the firms in the merger had committed all of its economically-recoverable coal, and so its disappearance by merger did not remove from the market any competitive force that could be preserved by enjoining the merger.

Ball Memorial Hosp., Inc. v. Mutual Hosp. Ins., 784 F.2d 1325, 1336 (7th Cir. 1986). Any other result would be inconsistent with the principal objective of Section 7, namely, the prevention of mergers that lead to the reduction of output. *Hospital Corp. of America v. FTC*, 807 F.2d 1381, 1386 (7th Cir. 1986), *cert. denied*, 481 U.S. 1038 (1987).

Despite its unusual facts, this Court and others have interpreted *General Dynamics* to stand for the proposition that reliance upon historic market shares as evidence of a merger's anticompetitive effects is inappropriate where, *for whatever reason*, the market share overstates a firm's future

competitive significance and, thus, overstates the anti-competitive effects likely to flow from the merger in question.[7] Indeed, the former Director of the FTC's Bureau of Competition, Kevin Arquit, merely ten months before the panel's decision, stressed that the *General Dynamics* doctrine is most applicable "where the firm at issue suffers inherent structural weakness." Kevin Arquit, Remarks Before The American Bar Association, *The Failing Firm Defense and Related Issues* 24 (April 12, 1992).

Thus, the panel erroneously held that the technical inability to *make* a product has no bearing upon a firm's competitive significance in the marketplace since a firm can always rely upon another firm (even a competitor) to manufacture for it or supply it with the critical inputs that it cannot make. (App. 26a) In reaching this conclusion, however, the panel ignored the fundamental economic principle underlying *General Dynamics*, i.e., that the ability to control output, not a mere presence in the market, is the basis for a firm's competitive significance. Gregory J. Werden, *Market Delineation and the Justice Department's Merger Guidelines*, 1983 Duke L.J. 514, 521; *see Ball Memorial, supra* note 7. Absent such an ability, a firm cannot exert any independent influence in the market, and its elimination by merger can have no anticompetitive effect. *See Citizens & Southern; Ball Memorial.*

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[7] *See United States v. Citizens & Southern Nat'l Bank,* 422 U.S. 86, 120-21 (1975); *Ball Memorial Hosp.,* 784 F.2d at 1336; *FTC v. National Tea Co.,* 603 F.2d 694, 700-01 (8th Cir. 1979); *United States v. International Harvester Co.,* 564 F.2d 769, 773-74 (7th Cir. 1977); *United States v. Consolidated Foods Corp.,* 455 F. Supp. 108, 137-39 (E.D. Pa. 1978).

Underpinning the panel's misunderstanding of *General Dynamics* is the panel's economically erroneous assumption that Olin's dependence upon a competitor for a critical input did not affect Olin's competitive significance. For some unexplained reason, the panel ignored a prior holding of the Ninth Circuit recognizing that "[e]very supplier of goods and services is . . . dependent on the efficiency and goodwill of upstream suppliers [and] [a]bsent structural constraints that keep competition from performing its levelling function, few businesses can dictate terms to . . . suppliers with impunity." *United States v. Syufy Enters.*, 903 F.2d 659, 671 (9th Cir. 1990).

In the instant case, it is axiomatic that the undisputed absence of a competitively structured CA merchant market allowed Nissan to charge Olin monopoly prices for CA—if it chose to continue to deal with Olin at all. *See Berkey Photo, Inc. v. Eastman Kodak Co.*, 603 F.2d 263, 272 (2d Cir. 1979) ("There is little disagreement that a profit-maximizing monopolist will maintain his prices higher and his output lower [than] the socially optimal levels . . . ."), *cert. denied*, 444 U.S. 1093 (1980).[8] In reality, as the only unintegrated isos producer, Olin could not be a competitive producer of isos. *See In re B.F. Goodrich Co.*, 110 F.T.C.

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[8] As Professor Areeda and others have explained, a firm in Nissan's position would be able to reap the entire monopoly profit on its sale of CA to Olin without regard to competition in the downstream sale of isos. Phillip Areeda & Donald F. Turner, *Antitrust Law* ¶ 725b (1978); *Town of Concord, Mass. v. Boston Edison Co.*, 915 F.2d 17, 23-24 (1st Cir. 1990), *cert. denied*, 499 U.S. 931 (1991); Herbert Hovenkamp, *Economics and Federal Antitrust Law* 199 (1985). *Cf. Jefferson Parish Hosp. Dist. No. 2 v. Hyde*, 466 U.S. 2, 36 (1984) (O'Connor, J., concurring) (vertical integration cannot increase monopoly profit).

207, 321 n.174 (1988) (unintegrated producers cannot compete with integrated producers if the costs of key inputs are consistently lower than the price at which the unintegrated firm can purchase that input). Nissan's ultimate control over Olin's output of isos by controlling Olin's CA supply thus requires a conclusion that Olin's acquisition of FMC's isos business did not reduce the number of independent isos producers and did not substantially lessen competition under Section 7 of the Clayton Act.

Ironically, the panel's reasoning that Olin's ability to purchase crucial inputs from its competitor rendered it the equivalent of an independent, integrated producer of isos applies with equal force to the *General Dynamics* case itself. Nothing prevented General Dynamics from purchasing coal from its competitors and reselling it. Yet, as this Court no doubt realized, such reselling would leave the ultimate control of General Dynamics' output in the hands of its suppliers, and therefore General Dynamics' "presence" in the market would be wholly illusory from a competitive standpoint.

In the same way, Olin's reliance upon Nissan for CA reduced Olin to a competitively unimportant isos producer. By refusing to acknowledge this reality of economic relationships, the panel limited the *General Dynamics* doctrine to its facts in contravention of the Seventh Circuit's holding that "the rationale of that case was not limited to situations involving limited amounts of a natural resource." *United States v. International Harvester Co.*, 564 F.2d 769, 773 n.7 (7th Cir. 1977).

Ultimately, the flaw in the panel's *General Dynamics* analysis is starkly revealed in the remedy it sustained. In upholding the FTC's order requiring Olin to divest the CA

plant it acquired from FMC, the panel expressly recognized that any firm that wished to be a viable isos producer had to have a captive CA source. *See infra* pp. 24–26. In the context of the *General Dynamics* doctrine, this acknowledgment should have led to the conclusion that Olin was never a competitively viable isos producer in the first place.

II. THE PANEL'S REJECTION OF ECONOMICALLY MEANINGFUL MARKETS DIRECTLY CONFLICTS WITH *BROWN SHOE* AND THE LAW OF OTHER CIRCUITS

The panel began its discussion of product market definition by stating that it could not determine in which market—isos or dry sanitizers—the FTC had found anticompetitive effects. (App. 7a) This concession, alone, required remand to the FTC and requires summary reversal in this case.[9]

More fundamentally, the panel's decision is erroneous because it upheld the FTC's definition of an economically meaningless market under Section 7 of the Clayton Act, i.e., "dry sanitizers." Thus, the panel failed to recognize the significance of the FTC's finding that "the price sensitivity between isos and cal hypo is not pronounced."[10] In addition, the panel did not even consider whether the

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[9] It is well settled that, where a court cannot determine the rationale of an agency's decision, it must remand to the agency for clarification. *Burlington Truck Lines, Inc. v. United States,* 371 U.S. 156, 167-68 (1962).

[10] FTC counsel did not challenge this finding. Instead, in oral argument before the FTC, FTC counsel conceded that at least a 15-20% increase in the price of cal hypo would be required to cause a significant number of consumers to shift to isos. (May 24, 1988 Transcript of Oral Argument 33).

approximately 100% price differential between isos and cal hypo required a finding that the two products lacked meaningful cross-elasticity between them.[11]

Instead, the panel baldly asserted that *Brown Shoe* allows a finding that products can occupy the same antitrust product market *even though meaningful cross-elasticity of demand is undisputably absent.* The panel stated:

> [A] finding of cross-elasticity is not precluded by the fact that a higher price increase is necessary to induce a switch [from cal hypo to isos]; a higher price increase indicates only that *the relationship between the two products is somewhat inelastic – but not necessarily so inelastic as to exclude the products from the same market, particularly under the substantial evidence standard of review.*

(App. 18a)(emphasis added).

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11 *See, e.g., United States v. E.I. du Pont de Nemours & Co.,* 351 U.S. at 401; *General Foods Corp. v. FTC,* 386 F.2d 936, 940-43 (3d Cir. 1967), *cert. denied,* 391 U.S. 919 (1968); *Reynolds Metals Co. v. FTC,* 309 F.2d 223, 229 (D.C. Cir. 1962) (Burger, J.); *Consolidated Gas Co. v. City Gas Co.,* 665 F. Supp. 1493, 1517 (S.D. Fla. 1987) (although natural gas and propane gas were functional substitutes, natural gas was a relevant product market because the price differential between the two was so substantial (100%) that consumers would not switch from natural gas to propane if the price of natural gas rose 5%), *aff'd en banc,* 912 F.2d 1262 (11th Cir. 1990), *vacated on other grounds,* 499 U.S. 915 (1991); *FTC v. Warner Communications Inc.,* 742 F.2d 1156, 1163 (9th Cir. 1984) (prerecorded music found to be a market where a 300% price difference existed between it and home taping); *In re B.A.T. Indus., Ltd.,* 104 F.T.C. 852, 931-32 (1984) ("[A] substantially and persistently higher price [for one of two products at issue] indicates that a small price change for either product would be unlikely to induce [switching].").

In so holding, the panel effectively found that there is no limit to the hypothetical price increase used to determine whether there is a meaningful cross-elasticity of demand between two products. Further, the panel rationalized that the *Brown Shoe* "indicia" of market definition can compensate for an undisputed lack of meaningful cross-elasticity of demand between two products.[12] This reasoning is a significant departure from decisions in other circuits and the Supreme Court.[13]

It is well-settled that two products can occupy the same market only if there is sufficiently high cross-elasticity of demand between them. *See, e.g., United States v. E.I. du*

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12 While *Brown Shoe* speaks of "reasonable interchangeability of use or the cross-elasticity of demand," 370 U.S. at 325 (emphasis added), it clearly treats the two terms as substitutes rather than complements. *Cf. United States v. Moore,* 613 F.2d 1029, 1040 n.85 (D.C. Cir. 1979) (collecting authorities where use of "or" rendered statutory terms interchangeable or conjunctive), *cert. denied,* 446 U.S. 954 (1980). Any other approach would overrule the holding in *E.I. du Pont* that "reasonable interchangeability" *is measured by* cross-elasticity of demand. 351 U.S. at 394-95. No case of which we are aware has read *Brown Shoe* to overrule *E.I. du Pont* in this manner. *See, e.g., Archer-Daniels-Midland,* 866 F.2d at 248 (despite absolute fungibility, products cannot be in the same market absent "high cross-elasticity of demand"), *cert. denied,* 493 U.S. 809 (1989).

13 If the panel were correct in relaxing the cross-elasticity test in *Brown Shoe* based on a functional view of reasonable interchangeability, it should have included liquid bleach in the market and defined the relevant market as all pool sanitizers. *See In re Heublein, Inc.,* 96 F.T.C. 385, 576 (1980) (finding an all wine market where there was "some significant competitive confrontation among even the most disparate wines"); *In re Coca-Cola Bottling Co.,* 93 F.T.C. 110, 204 (1979) (finding "no clear reason why [any wine] should be excluded from that continuum altogether, *given the clear interchangeability of end use with some products nearer the center*") (emphasis added).

Pont de Nemours & Co., 351 U.S. 377 (1956); *see also Kaplan v. Burroughs Corp.,* 611 F.2d 286, 291 (9th Cir. 1979) ("The principle most fundamental to product market definition is 'cross-elasticity of demand' for certain products or services."), *cert. denied,* 447 U.S. 924 (1980). To determine whether such cross-elasticity exists, a court must consider whether, in response to a hypothetical, small price increase in one product, a substantial number of consumers would shift to another. *Id.* Where such a price increase causes little substitution, any cross-elasticity of demand between the products is not meaningful and the products must be placed in separate antitrust markets. *United States v. Grinnell Corp.,* 384 U.S. 563, 573-75 (1966).

Until the panel's decision in this case, the Ninth Circuit had held on numerous occasions that only "economically significant" markets are relevant under the antitrust laws, irrespective of the similarities in form, use, or function of the products in question. As it explained in *International Telephone & Telegraph Corp. v. General Telephone & Electronics Corp.,* 518 F.2d 913, 932 (9th Cir. 1975):

> These [*Brown Shoe*] indicia were listed with the intention of furnishing practical aids in identifying zones of actual or potential competition rather than with the view that their presence or absence would dispose, in talismanic fashion, of the submarket issue. *Whether or not a court is justified in carving out a submarket depends ultimately on whether the factors which distinguish one purported submarket from another are "economically significant"* in terms of the alleged anticompetitive effect.

(emphasis added). *See also Thurman Indus., Inc. v. Pay 'N Pak Stores, Inc.,* 875 F.2d 1369, 1375 (9th Cir. 1989); *RSR*

Corp. v. FTC, 602 F.2d 1317, 1321 (9th Cir. 1979) (a market based on other indicia cannot be "justified" unless the product remains "economically significant"), *cert. denied,* 445 U.S. 927 (1980).

Moreover, prior to the panel's decision, there was no question what the Ninth Circuit meant by "economically meaningful" in the context of a cross-elasticity analysis. Specifically, in *State of California v. American Stores Co.,* 697 F. Supp. 1125, 1129 (C.D. Cal. 1988), *aff'd in relevant part, rev'd in part,* 872 F.2d 837 (9th Cir. 1989), *rev'd on other grounds,* 495 U.S. 271 (1990) (emphasis added), the court explained that "[p]roducts which are reasonably interchangeable are 'products to which consumers would switch if there were a *small but significant* non-transitory price increase' " (citation omitted). *See also In re Air Passenger Computer Reservations Sys. Antitrust Litig.,* 694 F. Supp. 1443, 1457 (C.D. Cal. 1988) (the "ultimate question" under the cross-elasticity of demand test is whether the availability of other products "significantly constrain[s] the price-raising power" of firms that produce the product in question), *sub. proceeding,* 727 F. Supp. 564, and *aff'd,* 948 F.2d 536 (9th Cir. 1991), *cert. denied,* 112 S. Ct. 1603 (1992); *Moore v. Jas. H. Matthews & Co.,* 550 F.2d 1207, 1218-19 (9th Cir. 1977) (absent demonstration of "extent

of cross-elasticity of demand," it is "impossible to determine" the extent of the relevant market).[14]

The great weight of judicial authority outside the Ninth Circuit also agrees that, absent a significant degree of cross-elasticity of demand, two products cannot occupy the same market. *See, e.g., Virtual Maintenance, Inc. v. Prime Computer, Inc.,* 957 F.2d 1318, 1325 (6th Cir.), *vacated on other grounds,* 113 S. Ct. 315 (1992); *United States v. Archer-Daniels-Midland Co.,* 866 F.2d 242, 248 (8th Cir. 1988), *cert. denied,* 493 U.S. 809 (1989); *Rothery Storage & Van Co. v. Atlas Van Lines, Inc.,* 792 F.2d 210, 218-19 (D.C. Cir. 1986), *cert. denied,* 479 U.S. 1033 (1987); *Photovest Corp. v. Fotomat Corp.,* 606 F.2d 704, 712-13 (7th Cir. 1979), *cert. denied,* 445 U.S. 917 (1980); *Consolidated Gas Co. v. City Gas Co.,* 665 F. Supp. 1493, 1517 (S.D. Fla. 1987) (5% test), *aff'd en banc,* 912 F.2d 1262 (11th Cir. 1990), *vacated on other grounds,* 499 U.S. 915 (1991).

The panel's decision is a radical departure from these established principles of product market analysis, principles applicable nearly to all antitrust cases. *See supra* note 2. Indeed, the panel's reasoning that there is no limit to the

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[14] Other circuits are in accord with this economically rigorous view of cross-elasticity. *See, e.g., Archer-Daniels-Midland Co.,* 866 F.2d at 248 & n.1 (absent "high cross-elasticity" products cannot occupy the same market); *Photovest,* 606 F.2d at 712-13 (products occupy separate markets where cross-elasticity is low); *see also Times-Picayune Publishing Co. v. United States,* 345 U.S. 594, 612 n.31 (1953) (products occupy separate markets where cross-elasticity is "small"); *SmithKline Corp. v. Eli Lilly & Co.,* 575 F.2d 1056, 1064 (3d Cir.) (absent "significant" cross-elasticity of demand, products occupy separate markets), *cert. denied,* 439 U.S. 838 (1978).

hypothetical price increase used to determine cross-elasticity of demand renders the cross-elasticity test meaningless; a large enough price increase will cause significant substitution away from *any* product. *United States v. Aluminum Co. of America,* 148 F.2d 416, 426 (2d Cir. 1945) ("[S]ubstitutes are available for almost all commodities, and to raise the price enough is to evoke them.")[15]

In upholding the "dry sanitizer" market, the panel apparently recognized that it was breaking with established precedent, but pressed on in deference to the substantial evidence standard of review. (App. 18a) Such deference is itself legal error, however, since this Court is bound to review, *de novo*, the legal standards applied by the FTC for defining the relevant market.[16] *RSR Corp. v. FTC,* 602 F.2d 1317, 1322-24 (9th Cir. 1979) (sustaining FTC's findings of fact regarding product and geographic markets and

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15 Thus, the panel's decision directly conflicts with those cases holding that, in performing cross-elasticity analysis, the relevant question is whether a "slight" or "small" price increase results in substitution from one product to another. *See United States v. Grinnell Corp.,* 384 U.S. at 571; *Archer-Daniels-Midland Co.,* 866 F.2d at 248 n.1 ("The appropriate question is whether a *slight increase* in the price of HFCS causes a considerable number of buyers of HFCS to switch to sugar.") (emphasis added)); *American Stores Co.,* 697 F. Supp. at 1129 ("small but significant nontransitory price increase" (citation omitted)); *Consolidated Gas Co.,* 665 F. Supp. at 1517 (5% test).

16 Administrative Procedures Act, 5 U.S.C. § 706 ("[T]he reviewing court shall decide all relevant questions of law . . . ."); *BOC Int'l, Ltd. v. FTC,* 557 F.2d 24, 28 (2d Cir. 1977) (content of actual potential competition doctrine under Section 7 a question of law on which court conducts *de novo* review).

holding that the FTC applied the proper legal test in evaluating those findings); *see also White & White, Inc. v. American Hosp. Supply Corp.*, 723 F.2d 495, 499-500 (6th Cir. 1983) ("[T]he district court's formulation of the market tests may be freely reviewed on appeal as a matter of law . . . ."). The panel thus erred in deferring to the FTC's legal conclusion that, even absent high cross-elasticity of demand, two products can occupy the same market. *See Archer-Daniels-Midland Co.*, 866 F.2d at 248 (ordering entry of summary judgment because, absent high cross-elasticity of demand, two products cannot occupy the same market).

This Court should reconfirm that the legal test for defining the relevant antitrust market is not to be compromised under the substantial evidence standard. It should also clarify the critical importance of defining only economically meaningful antitrust markets, whether the analysis is undertaken by a court or the FTC. Any other approach will leave the FTC free to choose whatever standard of market definition that will narrow or broaden the "market" in line with the FTC's desired outcome and lead to conflicting legal standards between the federal courts and the FTC. *United States v. Von's Grocery Co.*, 384 U.S. 270, 301 (1966) (Stewart, J., dissenting) ("The sole consistency that I can find is that in litigation under § 7, the Government always wins.").

III. THE PANEL HAD NO BASIS TO EXTRACT THE FTC FROM THE "CELLOPHANE TRAP"

Having stripped away the importance of the cross-elasticity principle in defining economically meaningful markets, the panel went on to sustain the FTC's finding of a "dry sanitizer" market based on circumstantial evidence

purporting to show that the prices of cal hypo and isos had converged somewhat in the mid 1980s. The FTC had found that such convergence had caused some consumers to shift from cal hypo to isos. (App. 41a)

The panel, however, agreed with Olin that the FTC had actually based the isos/cal hypo price convergence on the illegal dumping of isos by Japanese producers rather than on a natural result of substitution by consumers at historical market prices. (App. 16a) It is Olin's position that under these circumstances, any shift in consumer purchases from cal hypo to isos could not constitute circumstantial evidence of meaningful cross-elasticity of demand and in fact creates a variation of the analytical error known as the "Cellophane trap."[17] Indeed, the panel did not dispute that reliance upon evidence of cross-elasticity of demand within the confines of the "Cellophane trap" would be contrary to law. *Id.*

The panel rescued the FTC from the "Cellophane trap," however, by crediting the FTC's argument, adumbrated for the first time in its Appellate brief, that illegal dumping had occurred with respect to both isos and cal hypo to the same degree and with the same relative effect on price. (App. 17a) Thus, the panel concluded that meaningful cross-elasticity of demand existed between cal hypo and isos.

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17 *See Eastman Kodak v. Image Technical Servs., Inc.*, 112 S. Ct. 2072, 2084 & n.17 (1992) (high cross-elasticity at non-competitive price does not suggest that products occupy the same market); Phillip Areeda & Donald F. Turner, *Antitrust Law* ¶ 521b, at 353-54 (1978); William M. Landes & Richard A. Posner, *Market Power In Antitrust Cases,* 94 Harv. L. Rev. 937, 960-61 (1981).

Not only was the panel's rescue effort completely without a basis in the record,[18] it is also contrary to established principles of administrative law. The FTC's opinion did not discuss the "Cellophane trap"; indeed, in its Appellate brief, the FTC argued that the Cellophane fallacy does not apply when measuring cross-elasticities in a Section 7 case. Thus, the panel erroneously attributed to the FTC a rationale it could not have considered—something a panel may not do under the established principle that a court may not affirm an agency order based upon a rationale that does not appear in the agency decision. *SEC v. Chenery*, 318 U.S. 80, 87 (1943); *FTC v. Indiana Fed'n of Dentists*, 476 U.S. 447, 454-55 (1986) ("Once the Commission has chosen a particular legal rationale for holding a practice to be unfair, however, familiar principles of administrative law dictate that its decision must stand or fall on that basis, and a reviewing court may not consider other reasons why the practice might be deemed unfair."). Summary reversal of the panel's decision is therefore warranted.

IV. THE PANEL HAS SANCTIONED OVERBROAD AND INCONSISTENT DIVESTITURE REMEDIES

The panel apparently agreed that a remedial order under Section 7 must be tailored to alleviate the likely anticompetitive effects in the market, *see RSR Corp. v. FTC*, 602 F.2d 1317, 1325-26 (9th Cir. 1979), *cert. denied*, 445 U.S. 927 (1980), and must not be punitive or confiscatory in nature. *See United States v. E.I. du Pont de Nemours & Co.*, 366 U.S. 316, 326 (1961). However, the panel grossly

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[18] The subject of Japanese dumping was only part of the record as it related to the issue of ease of entry by Japanese producers. The record contains no evidence to the effect of cal hypo dumping on cal hypo prices; thus there is no evidence to support the panel's conclusion.

misapplied these standards since divestiture of Olin's CA facility is unrelated to the acquisition's purported anti-competitive effects in the dry sanitizer market.

In particular, the conclusion that a captive source of CA is necessary to ensure viability of the divested entity is directly at odds with the panel's holding, debunked earlier, that *Olin* itself was a competitively viable isos producer *without* such a source. In response to this argument the panel found that *ensuring* a new entity's future viability is not *necessarily* inconsistent with the historical fact of Olin's purported viability. (App. 27a) The necessity of such ensurance, however, only highlights the absence of a merchant CA market, an absence that rendered Olin dependent upon the benevolence of its competitors for a critical input. And a firm totally dependent upon its competitor for a key input cannot be *fully* viable under the *General Dynamics* doctrine.

More fundamentally, while the panel held that such divestiture would "ensure" the viability of the divested entity as an isos producer, such viability is unrelated to preserving the competitive structure of the market since it can only occur at the expense of Olin's own presence as a competitively viable isos producer. Indeed, it cannot be overlooked that ordering divestiture of the CA plant in 1994 is premised on the *current* availability of a CA supply relationship with Nissan that existed between 1981 and 1984, and a 1984 contract manufacturing agreement with Monsanto that the FTC viewed as anticompetitive. (App. 65a-68a) Therefore, if the panel wished to alleviate the anti-competitive effects of the transaction, it should have consid-

ered the anticompetitive consequences of sending Olin off to establish relationships with competitors that may no longer be available.[19]

As it stands, the FTC's remedy directly conflicts with the principle that the removal of one firm and substitution of another cannot increase competition. *Cf. Brunswick Corp. v. Riegel Textile Corp.*, 752 F.2d 261, 267 (7th Cir. 1984), *cert. denied*, 472 U.S. 1018 (1985) (proposed remedy transferring monopoly from one competitor to another suggested that lawsuit had nothing to do with preservation of competition). The panel's affirmance of the divestiture of Olin's CA facility thus simply renders Olin the loser in a zero-sum game, a clearly punitive result.

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[19] At a minimum, the panel should have remanded the case for a hearing to determine whether divestiture of Olin's CA plant will leave Olin without the ability to produce or sell isos at all.

CONCLUSION

To permit the panel's decision to stand would clash with Supreme Court precedents and with decisions of other circuits. It would also eviscerate much of the economic rigor brought to antitrust analysis by this Court in all antitrust analysis and would seriously undermine the predictability that is needed in federal antitrust enforcement by creating inconsistent legal standards between the FTC and the federal judiciary.

Respectfully submitted,

/s/ Neal R. Stoll

Neal R. Stoll
Counsel of Record
James A. Keyte
Alan J. Meese

Skadden, Arps, Slate,
Meagher & Flom
919 Third Avenue
New York, New York 10022
(212) 735-3000

Counsel For Olin Corporation

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